STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

4. The **return on current asset value component** will be determined as the per patient day return on value, where the return on value will be a "tenure factor" times the lesser of "current asset value" or the "current asset value upper limitation." Current asset value will not be allowed to diminish below the "current asset value floor" (terms as defined below).

a. The **tenure factor** is based upon a provider's number of years of continuous licensure determined at the beginning of the provider's rate year and the number of calendar days in the provider's cost reporting period from which asset values and patient days are determined. Beginning with rate years starting on or after October 1, 1990, the tenure factor will be 2.5 percent for less than two years of ownership tenure and increase 0.25 percent per year of tenure up to 5.25 percent for 12 or more years of tenure. The tenure factor is the percentage determined above times the ratio of days in the provider's cost reporting period to 365 days. Licensure tenure will be based upon the number of full years that have elapsed from the effective date of a provider's license issued by the Michigan Department of Public Health to the beginning of the provider's rate year. **Exception:** In the situation where licensure has changed but there has been no effective change in operator/provider and there has been no transaction which would affect Medicaid reimbursement other than the tenure factor, the provider may petition the State agency to recognize the continuous tenure (i.e., the licensure tenure schedule would not revert to zero years at the time of licensure change if the petition is approved).

b. The **current asset value** is determined by a formula using historical costs of capital assets times the difference between an inflationary index and an obsolescence factor. Assets purchased prior to 1960 will be treated as if they were brought into service in 1960.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

1) The historical cost of capital assets will be based upon the initial owner's audited historical acquisition cost determined as allowable in accordance with Medicare Principles of Reimbursement as modified by Section III. It will be the responsibility of the current asset owner to provide the audited historical acquisition cost and purchase date information of the initial owner, otherwise the assets will be assumed obsolete for payment determination purposes (i.e., no current asset value). An exception to the historical acquisition cost basis is allowed for land which will be based upon the current owner's acquisition cost not to exceed the amount reported to the Internal Revenue Service for federal taxation purposes. Leased or rented assets, when the underlying audited historical acquisition cost to the initial owner has not been disclosed, will be treated as an obsolete asset for payment determination purposes.

At the discretion of the single State agency, in the determination of historical acquisition cost of capital assets, cost information from other sources will be considered. These sources include, but are not limited to Medicare or Blue Cross/Blue Shield reports or a provider's initial Medicaid report. To ensure the Program does not continue to pay for assets that no longer exist, the original acquisition costs of movable equipment and fixed building equipment items that are replaced will be removed from the determination of current asset value in the year the replacement was made. For other asset items, which have been replaced, renovated or improved and reported as a cost in cost report periods ending March 31, 1985 and thereafter, the original acquisition costs or an estimate thereof will also be removed from the determination of current asset value.

An exception to the above methods for capital assets may be made for the costs associated with the centralized facilities of related organizations. The plant and variable costs of such organizations will be treated as purchased services (variable costs) unless the related organizations' financial records assign the assets to the specific facilities. Another exception to the historical acquisition cost basis may be allowed for the occasional purchase of used movable equipment by ongoing operations when the purchase is not part of a change in facility ownership.

STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

For facilities converting to the tenure method, effective with facility fiscal years beginning on or after April 1, 1991, as a result of the elimination of grandfather plant reimbursement provisions described below, the determination of an unacceptable basis for calculation of current asset value will be appealable, for a limited time, under Section VIII of this plan. The appeals period for an affected facility is limited to January 1, 1991 through the beginning of the facility's fiscal year affected by the change. In appealing the determination of current asset value, the provider must present evidence documenting a proposed higher asset valuation. Providers eligible for appeal will not be converted from grandfather provisions until an appeal determination has been rendered.

2) The inflationary index utilized depends upon capital asset type: land improvements, building, building improvements and fixed building equipment will be updated using the Marshall Swift Valuation Service Construction Cost Index for Class A Buildings in the Central United States from the fiscal year the asset was brought into service until the most recent period for which data is available when the rate is determined; and land, movable equipment and other assets will have an inflationary index of 1.00, i.e., no update factor.

3) The obsolescence factor utilized also depends upon the capital asset type: land improvements, building, building improvements and fixed building equipment will have an obsolescence factor of 3 percent per annum for each year the asset has been in service; movable equipment and other capital assets will have an obsolescence factor of 10 percent per annum for each year the asset has been in service up to a maximum of 10 years (this factor will not be greater than 1.00); and land will have an obsolescence factor of zero. The number of years the asset has been in service will be based upon the number of years including the fiscal year after the year in which the asset was acquired through the most recent audited year.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

4) The current asset value formula is the sum of current asset values for each distinct asset, where the current asset value of a distinct asset is the historical cost of that asset times the difference between the inflationary index and the obsolescence factor for the respective asset. Current asset values will be rebased annually based upon the most recent audited or reviewed cost report.

5) Only assets having a use related to patient care are to be included for reimbursement under the return on current asset value component. The cost finding and cost reporting methods, as defined in the State agency's cost reporting forms and instructions, apportion the provider's asset costs into the appropriate cost centers for reimbursement purposes.

6) Assets acquired after July 1, 1989 for training of nurse aides (as required by the Omnibus Reconciliation Act of 1987), are not included in the calculation of current asset values if the purchase of the asset was reimbursed as a nurse aide training expense.

c. The current asset value upper limitation is a limit placed upon current asset value per bed above which values are not recognized for reimbursement purposes. The per bed value of the upper limit is based upon a survey of construction and other purchase costs per bed of Class I and Class II nursing homes opened on or after January 1, 1975, with the historical costs updated through 1983 using the U.S. Department of Commerce Composite Construction Index. Annual updates subsequent to 1983 will be made using the Marshall Swift Index indicated in Section IV.A.4.b.2.

d. The current asset value floor is determined as 30 percent of the current asset value upper limit.

STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

5. Special Provisions: The plant cost component will be determined using special methods for Class I and Class II providers with either newly purchased facilities or newly participating facilities or existing providers with either a change of class or major additions, renovations, or new construction.

Special methods are required because there is no, or there is an inadequate, historical plant cost basis upon which to determine rates or rates are determined by different methods.

a. **Plant Cost Certifications:** Such providers are requested to certify and submit to the single State agency their expected allowable costs (in accordance with Medicare Principles of Reimbursement as modified by Section III) for interest expense, property taxes, leases, and historical asset acquisition costs. If approved, the agency will determine the provider's initial period plant cost component based upon the certified amounts using the principles described in Sections IV.A.1. through 4 above and IV.A.5.b. and c below. This rate will be retrospectively adjusted to reflect the facility's actual audited allowable plant costs for each fiscal year until the facility's rate is prospectively established from a cost reporting period which reflects a full cost reporting period of costs related to the original purpose of the plant cost certification. If, as a result of audit, the State agency finds a significant discrepancy between certified information and actual costs, all excess funds paid by the State agency to the facility as a result of that request will be recovered with a penalty factor (equal to the then current Medicare rate on net equity) applied to the discrepancy.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

b. **Sales and Resales:** In the event of a sale occurring on or after July 18, 1984, but not the result of a binding agreement entered into prior to July 18, 1984, the changes in the plant cost component for a facility, attributable to the sale will be limited by the increase allowed by Section 1902(a)(13)(B) of Title XIX of the Social Security Act in effect prior to the Consolidated Omnibus Budget Reconciliation Act of 1985. In cases where the Title XIX Section 1902(a)(13)(B) limitation is applicable, a schedule of interest expense disallowance amounts will be developed to ensure the new owner's reimbursement does not increase by more than the amount the Title XIX Section 1902(a)(13)(B) limitation will allow. The schedule of disallowances will be based upon the initial year disallowance and the borrowing amortization schedule and interest expense amounts determined as allowable costs in accordance with Medicare Principles of Reimbursement as modified by Section III of this plan. Once the schedule is put in place, the disallowances will remain in effect regardless of the status of the loan. However, in no instance will the amount of interest expense allowable exceed net allowable interest expense.

1) In all cases of sale or resale, the seller must notify the State agency at least 90 days in advance of the sale. The sale will not be recognized for reimbursement purposes until 90 days after notification. Any exception must be approved by the state agency.

2) Exception: Where licensure does not change subsequent to a sale, the lessee/provider must choose either to retain his original licensure tenure schedule and forego increased reimbursement for interest expense or to receive increased reimbursement for interest expense and allow the licensure tenure schedule to revert to zero years and a tenure factor of 2.5 percent. Should the lessee/provider elect to retain the previous licensure tenure schedule, the Medicaid Program will not recognize for allowable cost determination purposes, interest expense beyond the schedule of borrowing principal amortization and interest expenses which would have been incurred were the seller's loans maintained or assumed by the new owner/lessor. This provision will apply to all property transactions between lessors, lessees and/or operators.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

c. **Change of Class:** An existing provider becoming a Class I or Class II facility will be paid a plant cost component determined using the principles stated in Sections IV.A.1 through 4 above.

6. Grandfather Clause: Any provider who received a higher plant cost component under the reimbursement system in effect prior to April 1, 1985 may, at the option of the provider, be paid a plant cost component determined in accordance with Section IV.B. below until facility fiscal years beginning on or after April 1, 1991. If a grandfathered facility is sold subsequent to April 1, 1985, and there is a change in licensure, then the grandfather clause will no longer be applicable and the new owner's rate will be determined utilizing the methods in Sections IV.A.1 through IV.A.5 above. If a grandfathered facility is sold subsequent to April 1, 1985, and there is no change in licensure, then the grandfather clause may continue to be applicable until facility fiscal years beginning on or after April 1, 1991.

7. Special Note on Recapture of Depreciation: In the event of a sale after March 31, 1985, there will be the application of 42 CFR 413.134(f) for any reimbursement received by the seller as depreciation expense from October 1, 1984 through the effective date of the sale and transfer of assets.

B. Plant Cost Component (for Class III facilities and grandfathered Class I and Class II facilities)

The prospectively established plant cost component for county medical care facilities, hospital long term care units and facilities grandfathered in Section IV.A.6. above is the lesser of allowable per patient day plant cost or the per patient day plant cost limit, as described below.

1. The allowable per patient day plant cost is the sum of depreciation expense, interest expense, property taxes, and recognized lease costs (as defined in Section III.H) divided by total patient days, as derived from the most recent audited cost report.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

2. The per patient day plant cost limit is the amount that would be paid for a recently constructed and prudently financed facility. The calculation of this amount is based on a survey of homes actually built between January 1, 1975, and December 31, 1977, updated to June 30, 1978, using the U.S. Department of Commerce Composite Construction Index, as published in the Survey of Current Business. The value for depreciation expense is based on the mean of the surveyed values of depreciable assets and the mean depreciation rate for assets of similar type, determined by using straight-line depreciation with useful lives determined in accordance with §104.17 of the Provider Reimbursement Manual. The value for interest expense is based on the surveyed mean of interest rates paid and mean asset values for facilities constructed during the three years surveyed. The value for property taxes is based on the mean of property taxes of the surveyed tax-paying facilities. This plant cost limit is updated annually to reflect the rate of increase in property taxes and standards and regulations which affect plant costs.

3. Proprietary providers are permitted to retain as part of the plant cost component either:

   a. Up to $.50 of the difference between allowable per patient day plant costs and the March 31, 1985, 80th percentile of Title XIX per patient day plant costs ($5.66 per patient day), or

   b. The Medicare return on net invested equity defined in 42 CFR 413.157 to the extent that the plant cost component including the return on equity does not exceed the provider's plant cost limit.

   Once option (b) is selected, a provider may not select option (a) for any future cost reporting periods.

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STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

4. Special Provisions: The plant cost component will be determined using special methods for Class III providers with newly purchased facilities or newly participating facilities or a change of class. Special methods are also required for Class III and grandfathered Class I and Class II providers with major additions, renovations or new construction. Special methods are required because there is an inadequate historical plant cost basis upon which to determine rates or rates are determined utilizing different methods.

   a. Plant Cost Certification: Such providers are requested to certify and submit to the State agency their expected plant costs. The State agency will use the certified expected dollar value of plant costs, when approved, in calculating the prospective rate, pending audit. This rate will be retrospectively adjusted to reflect the facility's actual audited allowable plant costs for each fiscal year until the facility's rate is prospectively established from a cost reporting period which reflects a full cost reporting period of costs related to the original purpose of the plant cost certification. If, as a result of audit, the State agency finds a significant discrepancy between certified information and actual costs, all excess funds paid by the State agency to the facility as a result of that request will be recovered with a penalty factor (equal to the then current Medicare rate on net equity) applied to the discrepancy.

   b. The plant cost limit (PCL) for these facilities will be calculated based on one or both of the following principles:

      1) The per patient day plant cost limit will be updated to reflect changes in costs of construction, and changes in standards and regulations which have a direct impact upon plant costs. Costs of construction will be updated using the Department of Commerce Composite Index, as published in the Survey of Current Business.

      2) The per patient day plant cost limit will be updated to reflect changes in interest rates. The interest rate used to calculate the PCL will be updated by applying an index of change in interest rates for home mortgage loans (as reflected in conventional new home mortgage rates, as published by the Survey of Current Business) to the interest rate used to calculate the original PCL (Section IV.B.3. above).

STATE PLAN UNDER TITLE XIX OF THE SOCIAL SECURITY ACT
State of Michigan

POLICY AND METHODS FOR ESTABLISHING PAYMENT RATES
(LONG-TERM-CARE FACILITIES)

c. New Providers: A "new provider" is defined as a LTC provider in a facility that does not have a Medicaid historical cost basis and that has not provided care to Medicaid clients for a period of at least two years. The new provider's initial-period plant cost component will be the provider's certified and agency approved plant cost per patient day (per Section IV.B.4.a.) up to the plant cost limit, where the plant cost limit is determined using update methods 1) and 2) of Section IV.B.4.b. above.

d. Additions, Renovations, and Newly Constructed Facilities: The provider's initial plant cost component subsequent to the changes in plant costs will be the provider's certified and agency approved plant cost per patient day (per Section IV.B.4.a.) up to the plant cost limit, where the plant cost limit is the weighted average (using proportions of historical cost) of the historic PCL for the portion of the facility that remains unchanged, and the PCL applicable to the new portion, determined using update methods 1) and 2) of Section IV.B.4.b. above.

e. Sales and Resales: Sales and resales will be recognized by the program. Reimbursement for providers with facilities purchased prior to July 18, 1984, will be determined in accordance with the State Plan methods applicable at the time of sale. Reimbursement for providers with facilities purchased on or after July 18, 1984, but not the result of a binding agreement entered into prior to July 18, 1984, will use as a plant cost basis, allowable cost as determined in accordance with the Medicare Principles of Reimbursement as modified Section III. In all cases of sale or resale, the seller must notify the State agency at least 90 days in advance of purchase. The sale will not be recognized for reimbursement purposes until 90 days after notification. Provisions of 42 CFR 413.134 (f) will be retrospectively satisfied at this time. Any exception must be approved by the State agency. In the event of sale there will be an application of 45 CFR.134.(f) for any reimbursement received by the seller as depreciation expense from October 1, 1984 through the effective date of the sale and the transfer of assets.

The provider's plant cost component subsequent to the sale will be the provider's certified and agency approved plant cost per patient day (per Section IV.B.4.a.) up to the plant cost limit determined using update method 2) of Section IV.B.4.b. above (only the interest portion of the limit is updated).